NATIONAL CREDIT UNION ADMINISTRATION

NCUA News

November/December 2001
Number 8

HIGHLIGHTS

Board actions, November 15, 2001

RegFlex will assist most credit unions

The NCUA Board voted to issue the RegFlex rule, Chairman Dollar's initiative to significantly reduce the regulatory burden of well-capitalized, well-run credit unions, after the agency received a record 1,400 letters, most overwhelmingly supporting the new exemption rule.

"I believe RegFlex is the right approach at the right time to create a more empowering regulatory environment for America's credit unions while still emphasizing safety and soundness," said NCUA Chairman Dennis Dollar. "We need to get away from a one-size-fits-all approach to regulation. Such an approach can become a stumbling block to innovation and ultimately to the long-term financial strength of many credit unions. RegFlex is both an incentive for ongoing strong financial performance while at the same time providing earned regulatory flexibility for those strong performers."

Effective March 1, 2002, RegFlex automatically exempts approximately 3,870 credit unions with 1 or 2 CAMEL codes and 9 percent net worth for two consecutive exams from all or part of specified NCUA regulations. Another 1,893 credit unions may apply for RegFlex because the rule also contains an application process for institutions that meet one of the criteria.

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U.S. Capitol, Oct. 17, 2001 – NCUA Chairman Dennis Dollar, Senator Trent Lott, and the chairman's wife, Janie Dollar, at the reception Senators Lott and Thad Cochran of Mississippi hosted at the United States Capitol to honor Chairman Dennis Dollar. Attendees included US Senators, Members of Congress, credit union officials and other Bush administration appointees.

Court dismisses ABA challenge

The United States Court of Appeals dismissed, November 9, 2001, the American Bankers Association suit against NCUA's field of membership regulation issued pursuant to the Credit Union Membership Access Act (CUMAA).

"The Court of Appeals' decision represents a tremendous victory for NCUA and credit unions, but most of all it is a decisive win for consumer choice," NCUA Chairman Dennis Dollar said.

"It is my hope that this unanimous ruling will end nearly two decades of legal conflict the banking industry waged against NCUA and America's credit unions," Dollar said. "I believe banking and credit union communities would be better served by moving efforts and resources from the courtroom to the streets of America."

Johnson nomination sent to the Senate

News briefs

NCUSIF equity level — The equity level of the NCUSIF was 1.30 percent at October 31, 2001. The equity level is based on the June 30, 2001, insured share base of $387 billion.

Credit union failures — Through October, 19 federally insured credit unions failed in 2001. Five merged with assistance and 14 have entered involuntary liquidation. Of the involuntary liquidations, three were purchase and assumptions. The cost of failures through October was $4.7 million.

Capitalization deposit adjustments and refunds — Deposit insurance invoices and refund statements were mailed to credit unions with assets of $50 million or more Sept. 14, 2001. Refunds of $827,400 were sent by electronic transfer in late September to credit unions with shares that declined in the first six months of 2001. Invoices for $276.1 million were issued to credit unions with increased shares.

Among regulations under review

Corporate Credit Unions - Part 704. A proposed regulation change was issued in September. The comment period closes December 20, 2001.

Investment rule – Part 703. Issued in October, comments are due by Jan. 24, 2002

Technical amendments. A proposed rule was issued in June addressing technical amendments to various parts of Part 700, the definitions section. The comment period closed August 20. A final rule is expected by year-end 2001.

Regulatory review This is an ongoing project to modernize and update our regulations. Our practice is to review one-third of our regulations each year. OGC completed its review of the second third of our regulations in August 2001.

Board actions expected in December

- Final rule - Reimbursement of guest travel expenses.
- Proposed rule - Retirement benefits for FCU employees.
- NCUSIF operating level for 2002

Alexandria, Va., Nov. 1, 2001 — Board Member Yolanda Wheat (center) with NASCUS Chair Jerri Lattimore and a former NASCUS Chair Sarah Vega at a meeting with state regulators to discuss the overhead transfer rate and other issues. The group agreed to continue open dialogue in a spirit of cooperation and outlined a plan to focus training in 2002 on the new risk-based exam program being implemented by the NCUA."

NATIONAL CREDIT UNION ADMINISTRATION

NCUA News

NCUA News is published by the National Credit Union Administration, the federal agency which supervises and insures credit unions.

Dennis Dollar, ***Chairman***
Yolanda T. Wheat, ***Board Member***
Geoff Bacino, ***Board Member***

Information about NCUA and its services may be secured by writing to the Office of Public and Congressional Affairs, or by calling 703-518-6300. News of what is happening at NCUA is available by calling 800-755-1030 or 703-518-6339.

Clifford R. Northup, *Director*
Office of Public and Congressional Affairs
Cherie Umbel, *Editor*
Barbara Walker, *Graphics*

National Credit Union Administration
1775 Duke Street
Alexandria, VA 22314-3428

FCU statute dictates NCUA funding

NCUA's operating fee and overhead transfer process is based on provisions in the *Federal Credit Union Act*.

Title I of the Act created NCUA as a federal agency in 1934 supported by the federal credit unions it chartered and supervised. When Congress passed Title II in 1970, creating the National Credit Union Share Insurance Fund (NCUSIF) and assigning NCUA the responsibility to administer and manage risk to the fund, NCUA's role and its basic business purpose fundamentally changed.

Title II amended Title I by listing NCUA's funding sources as fees and assessments as well as income earned on insured deposits levied on insured credit unions. Congress did not specify any preference for funding sources. A separate section discussing operating fees merely states that these fees "may be used to defray the cost of federal credit union examination and supervision."

Regulatory role affects funding

Prior to 1970, NCUA examinations were principally compliance oriented and included a calculation to determine if credit unions remained solvent. Title II directed NCUA to conduct examinations that suit share insurance purposes, adding safety and soundness evaluations.

In today's environment, the consequence is a larger portion of NCUA's role is risk management of the NCUSIF

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Board actions November 15, 2001

NCUA adopts $146.9 million 2002 budget and predicts a 2003 budget decline

The NCUA Board adopted a 4.55 percent budget increase for 2002, well below the average budget increase, and the Board predicated a budget decrease in 2003 based on increased efficiency and cost-cutting measures that include a reduction of 33.5 agency positions through attrition.

While position reductions will save the agency $3.28 million in 2002, an average 4.5 percent salary adjustment combined with geographic locality pay and benefits will add $4.05 million to the 2002 budget. The average change in locality rates is 1.01 percent nationwide. Merit pay will increase a total 3.49 percent, with 1.24 percent included over 9.7 months of 2002 and a one-time payment of 2.25 percent issued in March. Pay adjustment expenditures also include an additional $1.42 million for examiner career ladder promotions in grades 7/9/11 in FY 2002.

Several offices in headquarters will be consolidated in 2002 to focus activities and resources on the core business practices identified in NCUA's strategic plan. 2002 will begin with the phase-in of the risk-based examination program. Steps are being implemented to control the escalation of payroll and place strict accountability on department and regional budget issues.

Overhead transfer rate set at 62 percent for 2002 and 2003

The NCUA Board set the overhead transfer rate at 62 percent for 2002 and 2003 based on an analysis of last year's time survey using three different approaches to determine how much staff time is spent on insurance-related and non-insurance-related activities.

The analysis indicates examiners, who represent over 60 percent of NCUA's workforce, spent 70.85 percent of their core program time on insurance related activities. After applying three different assumptions for determining the rate for non-program time, applied to the projected distribution of examiner time for 2002, data results indicate a minimum of 62 percent and as high as 70 percent of NCUA resources will be devoted to insurance-related activities in 2002.

The Board also voted to return to a three-year review cycle for the overhead transfer. Data gathered on an ongoing basis in 2002 and 2003 will be used to determine the overhead transfer rate recommendation for 2004.

Operating fee increases

The NCUA Board increased the operating fee assessment by 4.36 percent to fund the basic cost of NCUA operations that is not supplied by the overhead transfer fee.

The asset dividing points will increase by 8.5 percent, the projected asset growth for federal credit unions in 2001. Based on the increases, federal credit unions with assets of $10 million will pay $2,334 in operating fees, an additional $97, while $50 million federal credit unions will pay $11,670, an additional $487 in operating fees.

Rulemaking petition denied

The NCUA Board denied a petition from **Boeing Employees' Credit Union** for rulemaking with regard to the overhead transfer rate. The Board determined that the overhead transfer action does not meet the definition for required rulemaking under the Administrative Procedure Act (APA).

Chartering actions taken

Charter conversion

The NCUA Board approved the request of $54.5 million **Greenville Federal Credit Union**, Greenville, S.C., to convert from an occupational to community-based field of membership able to serve the people who live, work, worship, attend school and businesses and other legal entities in Greenville County, S.C.

Charter expansion

The NCUA Board approved a community charter expansion for $202.5 million **SAC Federal Credit Union**, Omaha, Neb., permitting the credit union to expand its field of membership to include Cass, Douglas and Sarpy Counties, Nebraska, and Pottawattomie County, Iowa.

Adding an underserved community

The NCUA Board approved the request of $350 million **Ft. Bliss Federal Credit Union**, El Paso, Texas, to add the underserved area of El Paso County to its field of membership. El Paso qualifies as an underserved area based on income, unemployment and the high poverty level.

Maryland business loan rule approved

The NCUA Board approved the Maryland member business loan rule for the use of federally insured, state-chartered credit unions in Maryland.

PacCorp gains expanded investment authority

The NCUA Board granted an investment concentration waiver request to **Pacific Corporate FCU,** Honolulu, Hawaii, allowing the corporate to exceed the non-secured concentration limit of a single issuer to 100 percent of the sum of reserves and undivided earnings and paid-in-capital. NCUA currently has a similar corporate investment proposal out for comment.

Asset Management Critical

Mortgage rates were at the lowest level since 1968 and there is the potential for still weaker economy and more systemic shocks. It is clear the potential for shocks is beyond the experience of many credit union managers and old "rules of thumb," may not apply. CUs should be reevaluating their investment, credit, liquidity, and balance sheet management to ensure they can withstand additional shocks and have procedures to evaluate their risk more frequently than they have in the past.

Board actions October 18, 2001

Allowance for loan and lease loss guidance proposed

The NCUA Board issued a proposed Interpretive Ruling and Policy Statement (IRPS) to provide federally insured credit unions with improved guidance for estimating and documenting allowance for loan and lease losses (ALLL). The guidance clarifies and illustrates ALLL practices consistent with generally accepted accounting principles (GAAP).

NCUA seeks to adopt guidance similar to the recent policy statement issued by fellow federal financial agencies. The proposal includes the following key points —

- Credit union management is responsible for establishing appropriate ALLL and documenting their methodology.
- Credit union methodologies should conform to generally accepted accounting principles.
- Requirements are less burdensome for credit unions with homogenous pools of consumer and mortgage loans than those with larger balance, non-homogeneous loans.
- An independent review of management's methodology and documentation practices by the supervisory committee, internal or external auditors is emphasized.
- Illustrations are provided that may be helpful in enhancing ALLL estimation methods and documentation practices.

The comment period is 90 days.

Investment authority and practice revisions considered

The Board issued an advance notice of proposed rulemaking, with a 90-day comment period, to determine if changes are necessary to the investment and deposit rule, Part 703. Potential changes would apply to brokers and safekeepers and would provide more flexibility for CU investments.

Comments are sought on areas pertaining to broker requirements, safekeeper requirements, expanded investment authorities, limitations on accounts under discretionary control of an investment advisor, investment credit ratings, borrowing repurchase agreements, and purchasing options to offer equity-linked certificates of deposit.

Many changes considered would remove or reduce restrictions pertaining to investment authority, especially for those credit unions demonstrating sound risk-management programs. It includes possibly removing restrictions on currently prohibited investments, expanding limits on investments held with financial advisors and reducing restrictions on borrowing repurchase transactions.

A pilot program is also being considered that would allow federal credit unions to purchase equity options to offer dividends based on the performance of an equity index.

NCUA is also asking for input on how to make Part 703 more user friendly and if the current Q&A format is beneficial.

Charter actions taken

Underserved area added

The NCUA Board approved the request of $274 million **Hughes Federal Credit Union**, Tucson, Arizona, to add an underserved area to its field of membership, which includes the 487,000 people who live, work, worship or attend school and businesses and other legal entities located in the city of Tucson.

An NCUA Board action was required because the population of the area is above the regional director's delegated authority of 300,000 for a single political jurisdiction.

Community conversion appeals denied

The NCUA Board denied appeal requests from two Miami credit unions — $253.5 million **Dade County Federal Credit Union** and $105 million **Pan Am Horizons Federal Credit Union** — applying to convert from multiple-group to community-based charters to serve the approximate 2.3 million people in Miami Dade County.

The Board decision was based on the lack of evidence that Miami Dade County qualifies as a local community as that term is used in the *Federal Credit Union Act* and under the standards of IRPS 99-1.

Nashville, Tenn., Oct. 19, 2001 – NCUA Board Member Geoff Bacino (right) at the grand opening of the technical center at Tennessee Teachers Credit Union. Also officiating at the ribbon-cutting ceremony are Nashville Mayor Bill Purcell, Board Chairman of Tennessee Teachers CU John Younger, and Tennessee Teachers CU President/CEO Betty G. Hobbs.

America's Tragedy

Chairman Dollar visits New York City credit unions and Ground Zero

NCUA Chairman Dennis Dollar was briefed November 6 in New York City by leaders of the credit unions impacted by the World Trade Center disaster of September 11 along with NCUA Region I Director Layne Bumgardner, New York regulatory authorities and the state league.

The day began with a briefing from officials of credit unions who had offices in or near the World Trade Center — XCEL Federal Credit Union, Municipal Credit Union and USAlliance Federal Credit. Officials from the New York State Credit Union League and Empire Corporate Credit Union explained their experiences on September 11 and afterwards.

Manuel Kursky, Deputy Superintendent of the New York State Banking Department also briefed Dollar on the state's response to the tragedy, and officials from the Mayor's office provided Dollar and NCUA officials with a tour of Ground Zero.

"These credit unions have truly demonstrated heroic acts of service in their efforts to assist their members during this time of a personal and national tragedy," Chairman Dollar told the group. "While a number of credit union members have perished, many of these families have been able to count on their credit union for financial stability and assistance."

Municipal Credit Union Chairman Dominic Morelli, XCEL Federal Credit Union CEO James Wisnieksi and US Alliance Federal Credit Union Senior Vice Presidents Bruce Simons and Alfred Scipio briefed Dollar on their operations since September 11.

Municipal Credit Union serves over 300,000 members, including City of New York firefighters, police officers, and other municipal governmental employees. XCEL's field of membership includes federal employees and the New York and New Jersey Port Authority.

CEO Wisnieksi said he believes in NCUA's disaster plan requirement, noting how helpful their existing crisis plan was and how helpful Examiner Tom DeSantis had been to his credit union. Morelli said that by September 13 Municipal Credit Union had branches opened serving its members. Municipal Chief Financial Office Kam Wong noted that severe communications problems, such as out of service ATM networks, hampered member services for some time after September 11.

New York City, November 6, 2001 -- Chairman Dennis Dollar visits with numerous credit union officials. From the left are Bill Mellin, president/CEO, New York State CU League; Joseph Herbst, president, Empire Corporate CU; Dominic Morelli, chairman of the Board, Municipal CU; Thomas Siciliano, general counsel, Municipal CU; Alfred Scipio, senior vice president, US Alliance FCU; Chairman Dollar; Layne Bumgardner, NCUA Region I director; James Wisnieksi, president, XCEL FCU; Bruce Simons, senior vice president, US Alliance FCU; Kam H. Wong, chief financial officer, Municipal CU; Barry Grant, EVP Information Systems, Municipal CU; and Raymond Scanlon, chairman of the Board, XCEL FCU.

***New York City Ground Zero, November 6, 2001** — Chairman Dollar visits former site of the World Trade Center.*

USAlliance representatives said their most productive branch was destroyed and two sponsors relocated dispersing members over a wide area. The credit union plans to reopen a branch within six to nine months.

Raymond Scanlon, board chairman of XCEL FCU, mentioned the loyalty of XCELs members, noting membership has actually grown since September 11.

Two credit unions, FAA Eastern Region FCU and USAlliance FCU, lost branch offices September 11. All four credit unions were able to continue operations elsewhere or return to operations within 48 hours of the disaster.

Dollar expressed his gratitude for "answered prayers" that all credit union staff safely evacuated their lower Manhattan offices on September 11 and commended credit union staff and leadership for their commitment to extend credit and financial services to the victims' families. He also commended the New York State Credit Union League for its prompt action to establish a command center in Manhattan to coordinate assistance for the affected credit unions.

"As the victims' families deal with loss that most of us can only imagine, I truly believe that their ultimate hope for peace of mind will be enhanced by these good credit union folks extending a helping hand to their members and neighbors," Dollar said.

Larger credit unions post strong 3rd quarter results

Federally insured credit unions with assets over $50 million grew a significant 12.81 percent in the first nine months of 2001 while the number of institutions declined slightly, down from 1,558 to 1,547. These institutions represent 15 percent of federally insured credit unions and nearly 83 percent of federally insured credit union assets.

Through three quarters of the year, the asset size of larger federally insured credit unions increased by $45 billion. Some pertinent year-to-date changes through Sept. 30, 2001, derived from 5300 data submitted by federally insured CUs in excess of $50 million follows:

- Assets increased 12.81 percent, up from $351.7 to $396.8 billion;
- Cash and investments increased 28.61 percent, up from $96.9 to $124.6 billion;
- Loans increased 6.46 percent, up from $242.6 to $258.3 billion;
- Deposit savings increased 13.5 percent, up from $304.9 to $346.1 billion;
- Equity increased 8.9 percent, up from $38.8 to $42.2 billion;
- Delinquency ratio increased from .60 to .62 percent; and
- Loan to share ratio declined from 79.57 to 74.63 percent.

Credit unions saw a significant cash infusion in the first nine months of the year, with nearly every major savings category increasing by double digits. Money market shares, which has led share growth throughout 2001, saw the largest percentage increase, up 27.2 percent from $45.8 to $58.3 billion. Regular shares, the largest category of savings, grew 11.7 percent, increasing from $93.4 to $104.3 billion. Share certificates, another large category of savings, grew 12.7 percent, up from $88.3 to $99.5 billion

Loan growth moderated during the year and much of the growth in shares flowed into cash and investments. While mortgage loans showed continued growth in response to declining market rates, two loan categories declined at larger credit unions through September 30. Unsecured credit card loans declined 4 percent, down from $18.6 to17.8 billion and other unsecured loans declined, moving down 1.8 percent from $16.1 to $15.8 billion.

First mortgage real estate loans, the largest category of credit union lending, grew 12.1 percent, increasing from $68.6 to $76.9 billion, while other types of real estate loans grew 6.29 percent, up from $33.7 to $35.8 billion.

Annualized income figures also provide positive results through the third quarter. Gross income at credit unions over $50 million increased 7.63 percent, up from $28 to $30.1 billion and net income gained 5.8 percent, up from $3.6 to $3.8 billion.

Key ratios reflect the trends in financial data submitted by credit unions. The net worth ratio of larger, federally insured credit unions at Sept. 30, 2001, was 10.48 percent, gross income to average assets was 8.05 percent, and return on average assets was 1.01 percent. Membership in over $50 million federally insured credit unions increased 3.2 percent, up from 55.2 to 57 million people.

Study backs NCUA approach to overhead transfer

The method NCUA uses to calculate the overhead transfer, which covers agency expenses tied to insurance activities, was judged sound in an independent study conducted by the CPA firm, Deloitte and Touché.

"NCUA came out very well," Chairman Dollar said after reading the study. "Deloitte and Touché listened to the views of associations representing all our stakeholders and gave our process an extensive review based on the issues raised. They found that our focus on risks to the share insurance fund from dynamics such as diversification, concentration and increasing asset size is recognized in the overhead transfer calculation process.

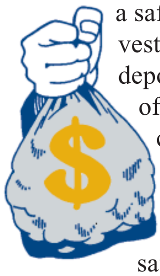
Deloitte and Touché was not asked to set the overhead transfer rate. Rather, they were asked to evaluate our methodology. NCUA utilized their findings to help establish an equitable rate. The Deloitte and Touché study found NCUA uses a cost allocation method that is "consistent with a multi-product company in the private sector." Their primary recommendation was that NCUA continue to update and conduct a thorough allocation process. NCUA will do so on an ongoing basis.

Nashville, Tenn., Oct. 2, 2001 —NCUA Chairman Dennis Dollar with Debbie Jones, loan officer, Dyersburg Credit Union, Dyersburg, Margaret H. Burton, manager, Progressive Teachers Credit Union, Chattanooga, and Bettie McCaskill, manager, Nashville Firemen's Credit Union following the Chairman's Open Forum in Nashville for Tennessee and southern Kentucky credit unions.

About investments

Use due diligence when purchasing CDs

Many credit unions purchase certificates of deposit (CDs) considering them a safe, secure easy way to invest funds because of federal deposit insurance. Irrespective of Part 703 requirements, credit unions may have a false impression that appropriate "due diligence" of CD brokers and safekeepers (custodians) is unnecessary when purchasing CDs. By failing to conduct comprehensive evaluations of CD brokers and safekeepers, credit unions are following unsound business practices.



Over the last few years, and again this year, credit unions lost money, received significantly delayed payments on matured CDs, and received unexpectedly lower interest rates on CD investments. Some credit unions also learned, after the fact, the CD they thought was an obligation of an insured depository institution was actually an uninsured obligation of a broker. Unforeseen, often costly surprises like these are unpleasant.

To avoid potential pitfalls and costly surprises, credit unions should conduct careful due diligence of brokers and custodians used to purchase and safekeep CDs. Recommended actions include:

- Check the status of counterparties with the National Association of Securities Dealers;
- Check appropriate federal and state bank regulatory authorities;
- Consult with other credit union colleagues;
- Ensure the safekeeper is a regulated entity independent of the broker.

After thorough investigation, choosing a single safekeeper for all investments can enhance safety and reporting and reduce overall costs.

To avoid potential pitfalls with CD brokers and custodians, credit unions should consider purchasing CD investments directly from issuing depository institutions.

RegFlex

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Chairman Dollar noted that the program does not target specific sized credit unions. In fact, 69 percent of the credit unions automatically eligible are under \$20 million in assets and 54 percent are under \$10 million.

Under Part 742, RegFlex credit unions are exempt from all or part of the provisions of the following NCUA Regulations:

- Section 701.36(a),(b) and(c) - FCU Ownership of Fixed Assets.
- Part 703 - Investment and Deposit Activities (Various Provisions).
- Section 701.25 - Charitable Donations.
- Section 701.32(b) and (c) - Payment on Shares by Public Unit and Nonmembers.
- Section 701.23 - Purchase, Sale and Pledge of Eligible Obligations.

In conjunction, appraisal rule Part 722 was amended to increase the threshhold when federally insured credit unions must obtain an appraisal from \$100,000 to over \$250,000.

NCUA will notify credit unions that are eligible for RegFlex. NCUA regional directors are authorized to revoke this expanded authority in whole or in part.

FCU statute

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while the federal credit union compliance role evolves into an increasingly smaller function.

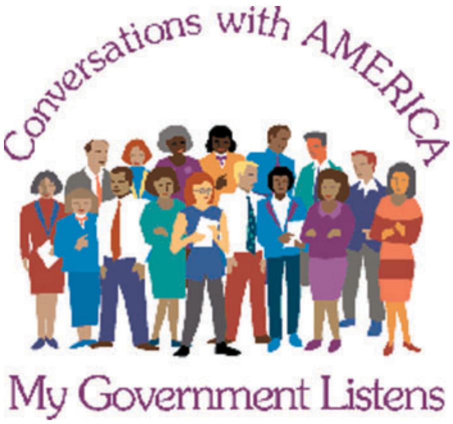
Congress authorized NCUA to fund the agency through two sources. Federal credit unions and federally insured state-chartered credit unions pay exactly the same cost for deposit insurance — a one percent deposit –while operating fees are determined exclusively by the respective supervisory organizations, state and federal.

How NCUA determines the overhead transfer rate

NCUA performs a careful, analytical analysis of time surveys completed by examiners to determine time spent on supervision and insurance related functions to ensure the NCUA Board sets a reasonable, fair overhead transfer rate.

Based on analysis of survey results, the 2002 NCUA budget will be funded by a 62 percent overhead transfer rate and federal credit union operating fees of \$51.25 million.

Warwick, R.I., Oct. 23, 2001 — NCUA Board Member Geoff Bacino at the Rhode Island Credit Union League Annual Meeting with Paul Archambault, president/CEO, Wave Federal Credit Union; Geoff Bacino; David Dupere, chairman of the Board, and president/CEO, Warwick Municipal Credit Union; and Robert Andrade, executive vice president/COO, Pawtucket Credit Union



Who and What: Chairman Dennis Dollar will speak at the National Association of State Credit Union Supervisors Conference
When: 8:30 a.m., Monday, Dec. 17, 2001
Where: Marriott Laguna Cliffs Resort, Dana Point, Calif.
Why: Participant feedback will be considered and solicited on NCUA initiatives or policies. Questions and answers with participants are scheduled.
Contact: Nicholas Owens at 703 518-6336 or nowens@ncua.gov

Who and What: Board Member Geoff Bacino will participate in NASCUS' Annual Conference & Symposium.
When: 11 a.m., Monday, Dec. 17, 2001
Where: Marriott Laguna Cliffs Resort, Dana Point, Calif.
Why: To represent the NCUA board and address the issues facing the credit union movement.
Contact: Dawn V. Woollen at 703-518-6318 or dwoollen@ncua.gov

Who and What: Chairman Dennis Dollar will speak at the Northern Virginia Business Development Roundtable
When: 1 p.m., Tuesday, Jan. 8, 2002
Where: Genesis Federal Credit Union, Springfield, Va.
Why: Participant feedback will be considered and solicited on NCUA initiatives and policies. Questions and answers with participants are scheduled.
Contact: Nicholas Owens at 703 518-6336 or nowens@ncua.gov

Who and What: Chairman Dennis Dollar will speak at the Northern Virginia Chapter of Credit Unions
When: 7:30 p.m., Thursday, Jan. 10, 2002
Where: PJ Skidoos Restaurant, Fairfax, Va.
Why: Participant feedback will be considered and solicited on NCUA initiatives and policies. Questions and answers with participants are scheduled.
Contact: Nicholas Owens at 703 518-6336 or nowens@ncua.gov

NCUA recommends CU exemption to FASB

The NCUA and credit union representatives have recommended to the Financial Accounting Standards Board (FASB) that implementation guidance for the new Statement of Financial Accounting Standard No.141, Business Combinations, include provisions allowing a merging credit union's GAAP retained earnings to transfer at point of combination.

NCUA told the accounting rule makers that if the purchase accounting model is not adjusted it would provide a disincentive to interested credit union merger partners, may thwart the survival of merging credit unions, and possibly increase costs to the National Credit Union Share Insurance Fund.

FASB requires all business enterprises to begin using the purchase method of accounting for combining businesses by mid-year 2001. However, the effective date of the new standard for credit unions and other mutual organizations is deferred in the short-term until FASB develops interpretive guidance related to the application of the purchase method to combinations of two or more mutuals.

Nineteen credit unions awarded CDFI funds

The U.S Treasury Department's Community Development Financial Institutions (CDFI) Fund announced its first group of recipients for Small and Emerging CDFI Assistance in October.

Among the 70 recipients, 19 community development credit unions were awarded nearly $2.4 million in technical and financial assistance of the total $8 million distributed. Credit unions can use technical assistance to support staff and management training, technology upgrades, and consultants for operational improvements.

Six credit unions received funds totaling nearly $1.7 million when the "Core" CDFI awards were announced in late September. Credit union Core and SECA awards totaled over $4 million in this round of distributions. Over $32 million in CDFI funding has been awarded to credit unions since 1996.

The assistance available through various CDFI programs includes secondary capital, financial (capital) grants, technical assistance grants, nonmember deposits and loans. Credit unions eligible to apply provide community development activities to targeted groups and investment areas. The goal is to build strong institutions that make loans and investments and provide financial services to economically-distressed investment areas and disadvantaged targeted populations whose need for loans, investments, and financial services are often unmet by traditional financial services.

The next application deadline for CDFI funding ends shortly. Credit unions can obtain applications for CDFI certification, Core Program, Small and Emerging Institutions (SECA) Program and Native American CDFI Technical Assistance (NACTA) Program from the CDFI website www.treas.gov/cdfi. The deadlines for filing applications for the various programs are:

- Dec. 11, 2001, for CORE;
- Jan. 24, 2002 for a SECA; and
- Jan. 24, 2002, for NACTA.

Credit unions should contact CDFI at 202-622-8662 for applications and program details.

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To place or renew a subscription, please complete then fax or mail the form below:

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Decal (in Spanish) - Adhesive (7"x3")	1076S	(8/00)	$ 1.00/2
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Federal Credit Union Bylaws	8001	(10/99)	$ 3.50
Federal Credit Union Handbook	8055	(1999)	$ 3.50
The Federal Credit Union Act	8002	(10/98)	$ 3.00
Federal Credit Unions (Leaflet)	8005	(5/96)	$ 7.50/100
NCUA Rules & Regulations-	8006	(11/01)	$20.00
Chartering and Field of Membership Manual	8007	(2000)	$ 6.50
NCUA User's Guide (Financial Performance Report)	8008	(2000)	$ .50
NCUA Examiner's Guide[1]	8018	(6/97)	$85.50
Your Insured Funds	8046	(12/00)	$14.00/50
Your Insured Funds (in Spanish)	8046S	(12/00)	$14.00/50
Yearend Statistics for Federally Insured Credit Unions	8060	(2000)	$ 5.50
Midyear Statistics for Federally Insured Credit Unions	8060	(2001)	$ 5.50
NCUA Credit Union Directory	8602	(00)	$15.00
A Guide to HMDA Reporting	9003	(1/98)	$ 5.00
HMDA Notice Poster	3222P	(6/97)	N/C
Supervisory Committee Guide for Federal Credit Unions	8023	(12/99)	$ 12.00
Suspicious Activity Report Form (2 diskettes per order)			
• Windows & User's Guide Software	9004	(7/96)	$ 10.00
• DOS & User's Guide Software	9005	(7/96)	$ 10.00
• Windows Package & Documentation	9006	(7/96)	$ 15.00
• DOS Package & Documentation	9007	(7/96)	$ 15.00
Subscription to NCUA Publications	9001	(1/00 - 12/01)	$125.00
		(7/00 - 12/01)	$ 62.50
FFIEC Information Systems Manual	9002	1996 Edition	$ 62.50
Vol 1&2			$ 50.00

[1]NCUA's Examiners' Guide is excluded from the Subscription Service.

Credit unions must actively monitor service providers

Credit unions increasingly partner with outside parties to enhance their member services, especially lending, where third-party relationships are opening doors to less traditional programs such as leasing, indirect lending, and risk-based or sub-prime lending.

Third-party arrangements can be cost-effective, enable credit unions access to expertise not available in-house and promote programs that may otherwise be unfeasible. However, there are cases of third-party relationships that resulted in financial stress due to unanticipated costs, legal disputes and asset losses. Generally, these situations occurred when the credit union either failed to exercise proper due diligence before entering a relationship or failed to set up controls to monitor performance.

Due Diligence Review

Credit union officials are responsible for planning, directing, and controlling credit union affairs. To fulfill these duties, officials should require a due diligence review prior to entering into any third-party arrangement. While not exhaustive, the following list identifies minimum due diligence procedures to follow:

Planning Officials should determine if proposed activities are consistent with the credit union's overall business strategy and risk tolerance. Potential risks include capital loss if the venture fails, loss of member confidence if the program doesn't meet expectations, and the costs tied to attracting and retaining qualified personnel and securing the necessary infrastructure.
Background Check — It is important to know how the third party has performed in other relationships. Contacting third-party clients is essential. Inquire how satisfied the clients are with your prospective partner and what pitfalls they may have encountered. The Better Business Bureau and Federal Trade Commission maintain complaint histories on businesses.
Legal Review — The credit union's attorneys should review all contracts to ensure that officials clearly understand the rights and responsibilities of each party.
Financial Review — Financial statements should be reviewed to determine the strength of the institution. Companies undercapitalized or with weak earnings may be unable to meet their contractural obligations. A licensed CPA audit will verify sound financial condition.
Return on Investment — The credit union should project its expected revenue, expenses, and net income from its investment and recognize how each of these factors may change.
Insurance Requirements — Third party relationships can result in increased liability. A thorough review of insurance coverage is necessary, including fidelity bond and coverage for errors and omissions, property and casualty losses, and fraud and dishonesty.
Controls —When a third-party arrangement is finalized, it is important a credit union establish controls to ensure the relationship is meeting expectations and the third party is meeting its responsibilities.
Policies and Procedures —The credit union should develop detailed policy guidance that states responsibilities, authorities, and reporting requirements. Limits should be established so that the program grows at a controlled pace and reflects the risk tolerance of the officials.
Staff Oversight — A credit union staff member should monitor program performance. Results should be compared to projections and performance should be reviewed to determine compliance with expectations and contracts.
Reporting — Reports should be submitted to the credit union's senior officials and directors to keep them abreast of significant findings, especially in areas of non-compliance.

Partnering with a third party to expand lending to members can lead to growth, improved profitability, and stronger member relationships. However, credit union officials are responsible for establishing appropriate due diligence procedures and a system of controls to ensure goals are met.

GC opinion letters

The NCUA General Counsel's Office issues opinion letters interpreting agency regulations and policies in response to questions submitted by the credit union community.

Secure the letters by contacting NCUA's Office of Public & Congressional Affairs, 1775 Duke Street, Alexandria, Va. 22314-3428 or by accessing NCUA's web site at www.ncua.gov/ref/opinionletters. Summaries of a few recent opinion letters follow.

01-742 — Sale of Non-deposit Investment Products – Federal credit union employees may sell non-deposit investment products to members for a credit union service organization or other third party if the program is structured to comply with the guidelines in NCUA *Letter to Credit Unions No. 150*.

01-0626 — Retention of investments following employee separation — A federal credit union (FCU) investing in the shares of a mutual fund for a particular employee benefit option plan may retain those shares for a limited time after employee separation, pending the employee's decision to exercise an option on the shares.

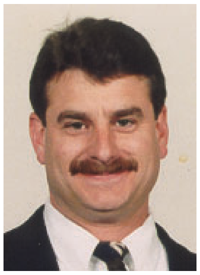
01-0775 — FCU offering custodian "omnibus account" for self-directed IRAs — The authority for FCUs to act as trustees or custodians for self-directed IRA and Keogh accounts appears in Part 724 of NCUA regulations. Determining if an omnibus account is permissible comes under the purview of the IRS, SEC and applicable laws.

01-0869 — FCU as licensed insurance agent — An FCU may provide its members the opportunity to purchase a third-party vendor's insurance products as a permissible finder activity under the NCUA incidental powers rule and become a licensed insurance agent, if required under state law, in order to act as a finder of insurance products.

01-0936 — Using a trade name without "federal credit union — An FCU may advertise its financial services using a trade name that does not include "federal credit union."

Keith Morton named Austin ARDO

Veteran NCUA manager named Region V associate regional director of Operations



The NCUA Board has selected agency veteran C. Keith Morton associate regional director of Operations (ARDO) in the Austin regional office. As Region V ARDO, Morton will be responsible for managing the in-house operations of Insurance, Supervision, Special Actions, and Management Services.

Morton began his NCUA career in December 1986 as a field examiner in Washington, D.C.

He spent the past seven years in management roles in the Region II office as a supervisory examiner, director of Special Actions and most recently director of Supervision. Morton has also served extended details as both ARDO, and ARDP, associate regional director of the field program in Region II.

Recent legislation

New anti-terrorism and money laundering law signed

President Bush signed into law October 27, 2001, an anti-terrorism and international money laundering bill that adds some new, specific money laundering provisions applicable to NCUA and credit unions, which are highlighted below:

- Credit unions are added to the institutions covered by the anti-money laundering statute.
- The Secretary of the Treasury will consult NCUA when establishing special due diligence for correspondent accounts and private banking accounts.
- The Secretary of the Treasury will consult NCUA when establishing rules for financial institutions adopting anti-money laundering programs, while the Treasury will have exemptive authority in implementing the rules.
- NCUA, along with fellow financial regulators, will promulgate minimum standards used to verify and identify customers that apply to financial institutions when new accounts are opened.
- After the law has been in effect for 30 months, NCUA will report and recommend needed changes to money laundering laws and regulations.

Visit NCUA'S extensive web site at www.ncua.gov

Happy Holidays

NATIONAL CREDIT UNION ADMINISTRATION
NCUA News

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